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SUBJECT: GARCIA'S ECONOMIC PRIORITIES

REF: A) Lima 2323 B) Lima 2507 C) Lima 2532

¶1. (SBU) Summary: During a June 20 meeting with the Ambassador, President-elect Garcia's economic team detailed Garcia's short term priorities, including improving water quality and promoting agricultural exports from the Andes. These programs should begin shortly after the July 28 inauguration, and if progressing smoothly, will help APRA leaders in the upcoming November 30 regional elections. In the medium term, Garcia is looking to reform key government institutions, including the judicial system and SUNAT. Garcia is also focused on maintaining macroeconomic growth while encouraging new investment. End Summary.

¶2. (SBU) The Ambassador hosted a meeting on June 20 with Garcia's economic advisors, including Enrique Cornejo, principal advisor and author of the majority of APRA's economic proposals, Luis Revollo, Carlos Nunez, environmental advisor Jose Salazar and Jorge Menacho. During the meeting, Cornejo provided a detailed vision that spanned the breadth of the economy and current GOP national capacity, setting priorities within a strict timeline.

Garcia's Priority Programs

¶3. (SBU) Cornejo began the meeting by describing Garcia's short term priorities, which are all related to poverty reduction: building infrastructure, improving access to water (agricultural and drinking), promoting agricultural export capacity building in the highlands and "the South" - a reference to the many in Southern Peru who voted for Ollanta Humala. Garcia and his team should be able to develop, and announce these programs during the July inauguration. Garcia's medium term goal is institutional reform. Cornejo also emphasized the need to maintain macroeconomic stability and attract new investment.

¶4. (SBU) The Sierra Exportadora program, which seeks to promote the production of export oriented agricultural products in the highlands (Ref B) is an immediate Garcia priority. Cornejo noted that the Administration would begin a pilot of this program, which could easily be replicated quickly in 28 other sites. The incoming government's other agricultural priorities include improving the transport chains, especially the road infrastructure, and strengthening micro enterprises.

15. (SBU) The incoming Administration will also focus on the environment, immediately launching a reforestation program in Eastern Peru. This program will reforest 100,000 hectares while creating \$500 million in exports and 50,000 jobs. Cornejo and Environmental Advisor Jose Salazar described the need to revise the forestry concession law, and noted their extensive work with environmental NGOs to develop workable forestry management plans. Salazar also noted that Garcia plans to create a \$100 million fund to finance water projects, both for agriculture and drinking water. Donors and multilateral development banks will provide the majority of the financing, with the GOP providing \$10 million. Salazar claimed to be well along in securing commitments for the fund, but mentioned a desire for U.S. Environmental Protection Agency technical assistance for the fund's structuring and management plan. By November 30, stressed Cornejo and the other APRA participants, the water program needs to show some solid results. Salazar is coordinating with APCI (the GOP's technical cooperation agency) on the best projects to implement in the short term.

Timeline for Priorities

16. (SBU) Cornejo acknowledged that Garcia will not have a honeymoon period to develop his programs. He underlined that the APRA transition team, the outgoing Toledo Administration and foreign donors must work together to coordinate priorities before July 28. President-elect Garcia will announce his priority programs during his inauguration speech. Some of these programs, particularly those mentioned above, should already be in the implementation stage as a result of coordination with the outgoing government. Garcia hopes that these priority programs, which focus on eliminating poverty and providing access to potable water, will help win back APRA votes in the upcoming November 30 regional elections, particularly in the Southern Andes.

Continuing Macroeconomic Success

17. (SBU) Cornejo acknowledged that the Toledo government is leaving Garcia a stable macroeconomic situation. Although Toledo's management of the macro economy was good, Cornejo pointed out that high export commodity prices played a key role in increasing the value of exports. Peru now has to plan for the day when world metals prices drop. Cornejo said that Garcia wants to keep the deficit at one percent of GDP, but noted that the Garcia team would be speaking with the multilateral banks to explore how Peru's macroeconomic health could be maintained with some slight adjustments to debt ratios. Garcia also sees the need to manage public expenditures and will mention austerity in his inauguration speech. The new government must control public salaries in order to have funding for poverty reduction programs.

18. (SBU) Cornejo agreed with the Ambassador on the importance of the FTA in connection to their own national/domestic markets as well as to foreign markets. Cornejo reiterated that the United States Government and APRA need to work together to create a short and medium term agenda that includes FTA implementation and other common priorities.

Garcia's Plans for the Mining Sector

19. (SBU) We discussed the difficulties in the mining sector with the APRA Economic Team. Cornejo acknowledged that mining companies pay high taxes, but that municipalities have trouble accessing the mining canon. The canon is important to addressing poverty; the new Administration would seek to redress the imbalance in canon distribution that has led to complaints and a disconnect between the companies, the people and the municipal governments.

¶10. (SBU) Cornejo said the government would not interfere with the mining sector's tax stability agreements. He emphasized the popular sentiment that these firms were not paying taxes, or enough taxes, was wrong. But the public rightly complains of too little benefit from the canon and public budgets. He described a cultural problem in Peru, where municipal governments elect to do small, easy and symbolic projects, such as building a new municipal plaza or office, over more needed public works. The government instead must focus on regional projects that benefit the public.

Institutional Reforms

¶11. (SBU) Cornejo concurred with the Ambassador of the necessity to reform state institutions. Judicial reform is paramount, but the Garcia government must maintain the autonomy of the judiciary. Cornejo mentioned discussions with GOP Dispute Coordinator Aurelio Loret de Mola, noting how these disputes created difficulties for Peru and the rule of law. Cornejo also agreed with the AID Director on the need for alternative dispute resolution mechanisms, and observed the recent improvements in the AID-sponsored Lima Commercial Courts system.

¶12. (SBU) SUNAT, the GOP tax agency, was also singled out for reform. Cornejo had no complaint with SUNAT employee ethics, but observed that SUNAT's aggressive approach was not always in the best interests of the government or people, and had led to disputes with U.S. firms. Other reforms included making the Vice Ministry of Fisheries, currently under the Ministry of Production into a separate ministry. Cornejo also talked of the need to reform government procurement policies. The economic team acknowledged the importance of land titling, but also agreed with the continuing institutional challenges -- and great expense -- faced by the GOP and USAID in its efforts to work this issue.

Comment

¶13. (SBU) The possible win of a number of Humala supporters in many of the local and regional elections, with a resulting opposition front to the national government -- in which Garcia already does not have a Congressional majority -- makes November 30 critical for the poor voters who have supported Humala. Garcia will indeed have no honeymoon, and his July 28 speech will be compared with Toledo's ambitious promises and Garcia's past record of poor governance. We expect that the incoming government will move quickly to implement poverty reduction policies in the Southern Andes. We were impressed by Cornejo's openness in attributing what he sees as their major challenges and APRA's positive assessment of the macro economic situation they will inherit. Clearly, he views the United States government as an ally in moving Peru forward under Garcia.

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